SCS Agency
Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

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Bill Number: AB 1708

Related Bills: AB 773, AB 779 (1995/96)
Telephone: 845-3410
Introduced Date: 01/27/98

Attorney: Doug Bramhall
Sponsor:

SUBJECT: Employer Credit for Qualified Wages and Property/Qualified Training Program

SUMMARY

Under the Personal Income Tax Law (PITL) and the Bank and Corporation Tax Law (B&CTL), this bill would authorize a credit to taxpayers equal to 50% of the qualified wages paid or incurred during the taxable or income year. To qualify for this credit, the qualified wages must be paid to an employee enrolled in a training program approved by the state's Employment Training Panel (ETP).

Under the PITL and B&CTL, this bill also would authorize a credit to taxpayers equal to 6% of the amount paid or incurred during the taxable or income year for qualified property. Qualified property would be limited to property used primarily for training purposes in connection with the taxpayer's participation in a training program that is authorized by the ETP.

EFFECTIVE DATE

Both credits would apply to taxable or income years beginning on or after January 1, 1999, and before January 1, 2004.

QUALIFIED WAGE CREDIT

SPECIFIC FINDINGS

Federal law provides special tax incentives designed to encourage employers to hire or train specified individuals, usually the unemployed or those in need of additional training. Certain state tax incentives are allowed if certain individuals participate in such federal programs as the federal Vocational Education Act of 1963, Job Training Partnership Act (JTPA) and the Greater Avenues for Independence (GAIN) Program. California law makes reference to these federal programs in describing individuals qualified to participate in certain state programs. In addition to these special tax incentives, existing state and federal laws allow a deduction for business expenses, including employee salaries.

DEPARTMENTS THAT MAY BE AFFECTED:

____ STATE MANDATE ____ GOVERNOR'S APPOINTMENT

Board Position:	Agency Secretary Position:	GOVERNOR'S OFFICE USE
____ S ____ O ____ SA ____ OUA ____ N ____ NP ____ NA ____ NAR ____X____ PENDING	____ S ____ O ____ SA ____ OUA ____ N ____ NP ____ NA ____ NAR DEFER TO ____________	Position Approved ____ Position Disapproved ____ Position Noted ____
Department Director Gerald H. Goldberg 2/24/98	Agency Secretary Date	By: Date:

Existing state law authorizes hiring tax credits, as well as other business tax incentives, which are intended to encourage business expansion and hiring in designated economic development areas: enterprise zones, the Los Angeles Revitalization Zone, local agency military base recovery areas, the targeted tax area, and manufacturing enhancement areas.

California law created the ETP to fund training to meet California employers' needs for skilled workers. The program's emphasis is on creating new jobs and assisting those receiving unemployment compensation to transition into new jobs through training. The ETP is funded by a 0.1% tax on the wages subject to unemployment tax. The ETP has statutory authority to set the terms of participation in the programs it administers. The ETP administers several employment training and retraining programs, all of which require a minimum 100 hours of training and a minimum 90-day retention period after the completion of training. The ETP contracts with businesses and training agencies to provide training to eligible participants. An eligible participant is a person who, prior to beginning training or employment, was unemployed and either receiving unemployment insurance benefits or had exhausted eligibility for unemployment insurance benefits within the previous 52 weeks, or who is employed but is determined by the ETP to be likely to be displaced and therefore about to claim unemployment insurance benefits.

Under PITL and B&CTL, AB 1708 would allow an employer to claim a credit equal to 50% of the qualified wages paid or incurred to qualified employees during the taxable or income year. Qualified wages would constitute those wages paid by the taxpayer to an employee while the employee is undergoing training in a training program approved by the ETP and in accordance with a training contract. Qualified wages could not exceed 200% of the minimum wage during the qualified time period. The qualified time period excludes time required for continued employment after completion of the training. No credit would be allowed until all requirements of the qualified training program as specified in the contract have been completed.

AB 1708 would require that the credit be claimed in lieu of other credits or deductions. **This bill** would allow taxpayers to carry forward any excess credit and apply it to future tax years, until the credit is exhausted.

QUALIFIED PROPERTY CREDIT

SPECIFIC FINDINGS

Federal law provides special tax incentives designed to encourage taxpayers to invest in certain types of property.

Existing state law authorizes tax credits for the purchase of certain types of qualified property. Examples of these credits include the Manufacturers' Investment Tax Credit and credits for property purchased and used in certain economic development areas.

Under existing state law, the time and manner for making various elections are set forth in statute, regulations, case law, tax forms, and instructions. Generally, elections must be made by the due date (including extensions of time) of the tax return for the first year for which the election is effective.

Although returns can generally be amended at any time within four years from the time prescribed by law for filing the original return, generally elections are irrevocable. For some, the department has the statutory discretion to accept or deny an amended return that makes, changes, or revokes the election.

Under PITL and B&CTL, this bill would authorize a credit to employers participating in an ETP program equal to 6% of the amount paid or incurred during the taxable or income year for qualified property. Qualified property would be limited to property used primarily for training purposes in connection with the taxpayer's participation in the ETP program.

If the taxpayer is eligible to claim more than one type of credit with respect to the qualified property, **AB 1708** would require the taxpayer to make an election of which credit will apply to that qualified property.

AB 1708 would require that the depreciable cost of the property be reduced by the amount of any reimbursement paid under the Unemployment Insurance Code for acquiring the property but does not reduce the depreciable cost by the amount of credit allowed under this provision.

This bill would allow taxpayers to carry forward and apply excess credit amounts to tax liabilities in future years, until the credit is exhausted.

Policy Considerations

Recent legislation has replaced language that requires taxpayers, when expenditures qualify for more than one credit, to make an election with a provision limiting the taxpayer to one credit with respect to qualified expenditures. This change allows taxpayers to make the choice of which credit to take on either the original or an amended return. The qualified property credit under this bill would require taxpayers to make an election on the original return.

Implementation Considerations

Many ETP contracts are executed with consortiums, which in turn train employees of smaller employers. This bill does not address the issue of how an employer would claim the credit for training received through a consortium.

This bill would allow an unlimited carryover for the credits. Recently enacted credits have contained a limited carryover since credits typically are exhausted within eight years.

FISCAL IMPACT

Departmental Costs

This bill would not significantly impact the department's administrative costs.

Tax Revenue Estimate

Estimated revenue losses attributed to the proposed qualified wage and property credits are reflected in the table below.

Fiscal Year Cash Flow Effective 1/1/99 Enactment Assumed After June 30, 1998 $ In Millions				
	1998-99	1999-00	2000-01	
Qualified Wage Credit	(minor)	($13)	($15)	($16)
Property Credit	(minor)	($2)	($2)	($2)
Total	(minor)	($15)	($17)	($18)

Minor = loss less than $500,000

Tax Revenue Discussion

Qualified Wage Credit:

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

The revenue impact for this provision would be determined by the number of individuals that go through the Employment Training Panel, the amount of wages paid, the length of time (hours) in training and the average amount of credit applied against available tax liabilities.

This estimate was developed in the following steps. First, according to the ETP, approximately 31,000 retrainees enrolled during fiscal year 1996-97. Second, according to the same panel, the average training hours per employee is approximately 120 with an average hourly wage of $15.50. Therefore, for this analysis, we used the proposed limit amount of 200% of the minimum wage. Third, as established by the Industrial Welfare Commission, the minimum wage rate will be $5.75 per hour when this bill would become effective in January 1999. This number was adjusted to reflect the proposed limit of $11.50 per hour ($5.75 x 200%). Fourth, by multiplying these elements, it is projected that qualified wages would be approximately $43 million annually. Fifth, this number was adjusted to reflect the proposed credit amount of 50% of qualified wages, generating $21.5 million. Sixth, the deduction tax benefit under current law for qualified wages was calculated to be approximately $3.5 million annually. These steps resulted in a 1999 year estimated revenue loss of $18 million. It was assumed that 50% of these credits would be applied in 1999, or $9 million, and the remaining credits would be carried over to subsequent years until fully exhausted.

Qualified Property Credit:

The revenue impact for this provision would be determined by the cost incurred by taxpayers for qualified property, and the average amount of credit applied against available tax liabilities.

Based on information published by the ETP, the maximum number of employers in any one-year that would be eligible for the proposed credit is roughly 200. In any given year, the potential investment in qualified property by these employers could be significant. Roughly 50% of the employers with which the ETP has contracted are in Standard Industry Classification Codes (SIC Codes) representing manufacturing. Therefore, it is likely manufacturing employers would be eligible for the existing investment tax credit on certain training property under current law for purchases of what would be qualified property under this proposal. The manufacturer's investment credit also is a 6% credit and is in addition to deductions for depreciation of the cost of the equipment on which the credit is based.

Assuming that qualified taxpayers would invest $100 million annually in qualified property, credits generated would total $6 million. Further, assuming that 50% of the qualified businesses would qualify for the existing investment credit, available credits under this bill would be reduced to $3 million. Taxpayer liabilities would limit the portion of credits generated that could be applied. Assuming 50% of the credits available could be applied, revenue losses would be $1.5 million in the first year (1999).

BOARD POSITION

Pending.